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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

NOV 14 1994

In the Matter of

Implementation of Sections of
the Cable Television Consumer
Protection and Competition Act
of 1992: Rate Regulation

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

MM Docket No. 93-215

BELL ATLANTIC PETITION FOR RECONSIDERATION

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Introduction and Summary

The Commission should reconsider its decision to adopt a productivity offset of zero for use in the cable TV industry price cap formula,² and should instead adopt an offset that is equivalent to the one to be adopted in the Commission's ongoing review of the price cap plan for local exchange carriers.³

As the record in this proceeding demonstrates and the Commission repeatedly has acknowledged, the cable TV and telephone industries are rapidly converging, and both industries are, to an ever increasing degree, deploying the same technologies to provide the same mix of services in competition with one another. As a

¹ The Bell Atlantic telephone companies ("Bell Atlantic") are Bell Atlantic - Delaware, Inc.; Bell Atlantic - Maryland, Inc.; Bell Atlantic - New Jersey, Inc.; Bell Atlantic - Pennsylvania, Inc.; Bell Atlantic - Virginia, Inc.; Bell Atlantic - Washington, D.C., Inc.; and Bell Atlantic - West Virginia, Inc.

² *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 -- Rate Regulation*, MM Docket No. 93-215, Memorandum Opinion and Order (rel. Sept. 29, 1994) ("Productivity Offset Order").

³ See *Price Cap Performance Review*, 9 FCC Rcd 1687 (1994).

result, and as the Commission itself has recognized, future productivity growth levels experienced by companies in these previously separate industries should be comparable.

The Commission's order, however, disregarded this convergence and arbitrarily adopted a productivity offset of zero for the cable TV industry. It did so, moreover, despite the fact that the cable industry ignored repeated Commission requests for evidence of cable's productivity growth -- evidence uniquely within the control of the cable industry to provide. In fact, the cable industry not only failed to rebut the substantial record evidence that cable and telephone companies will experience equivalent rates of future productivity growth, but the one limited study that the cable industry did submit actually confirms that productivity growth for cable and telephone companies is comparable.

Under these circumstances, the Commission simply cannot arbitrarily adopt a lower productivity offset for use in cable's price cap formula than it adopts for telephone companies. Not only is this result contrary to the record in this proceeding, but it will skew investment incentives and artificially favor one competitor over another to the detriment of a competitive marketplace.

Procedural History

A brief review of the procedural history here reveals that the Commission has ignored substantial evidence supporting equivalent productivity levels between the cable and telephone industries and

instead capriciously rewarded the cable industry for its failure to provide productivity data called for by the Commission.

The Commission initiated this proceeding in response to passage of the Cable Act of 1992, which required that the Commission establish rules to govern rate regulation of cable service tiers offered by cable systems not subject to effective competition.⁴ In its initial notice of proposed rulemaking,⁵ the Commission proposed price cap regulation that it analogized to the price cap regulation of AT&T and the telephone companies.⁶ The Commission specifically sought comment on how directly changes in cable operating costs are reflected by changes in the Gross National Product-Producer Index ("GNP-PI").⁷ Although the Commission and other regulators traditionally make that type of comparison by means of productivity studies, the cable industry failed to submit such a study in response to the Initial Notice.

In its report and order on the notice,⁸ citing the price cap orders for AT&T and the telephone companies, the Commission determined that price caps are "an effective alternative to cost-

⁴ Cable Television Consumer Protection and Competition Act, Pub. L. No. 102-385, §§ 3, 9, 14, 106 Stat. 1460 (1992).

⁵ *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992*, 8 FCC Rcd 510 (1992) ("Initial Notice").

⁶ Initial Notice, 8 FCC Rcd at 522-23.

⁷ Initial Notice, 8 FCC Rcd at 523.

⁸ *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 -- Rate Regulation*, 8 FCC Rcd 5631 (1993) ("Report and Order").

of-service regulation" and mandated price cap regulation to govern changes in rates from initial regulated levels.⁹

The Commission's next notice of proposed rulemaking explicitly called for information needed to set an appropriate productivity offset:

An important consideration under any form of regulation that is based on the costs of production is how to take productivity gains, if any, into account. While we recognize that the GNP-PI automatically reflects certain productivity gains in the economy, it does not necessarily reflect the entirety of productivity gains experienced by cable operators. While productivity may be measured in several ways, it is our responsibility in this proceeding to consider whether to apply a productivity offset feature in the price cap mechanism for cable operators.¹⁰

Specifically, after citing the "insufficient information available in the record," the Commission called for industry studies relating to various productivity offset options including an offset analogous to the telecommunications industry.¹¹ In suggesting such an approach, the Commission noted that it "would provide an incentive for future efficiency gains and harmonize

⁹ Report and Order, 8 FCC Rcd at 5776, 5777. In evaluating the appropriate offset for the price cap formula, the Commission took notice of some of the similarities between the cable and local telephone industries including capital intensity, investment in local physical plant and lack of sensitivity to changes in energy costs. *Id.* at 5781.

¹⁰ *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 -- Rate Regulation*, Notice of Proposed Rulemaking, MM Docket No. 93-215, 74 Rad. Reg. 2d (P&F) 1247, ¶ 83 (footnotes omitted) (rel. July 16, 1993) ("July Notice").

¹¹ July Notice at ¶ 85.

incentives for converging technologies."¹² The cable industry failed to submit any productivity study in response.

Based upon substantial evidence submitted in response to the notice, which demonstrated that the convergence of industries will result in equivalent productivity growth,¹³ the Commission tentatively concluded that:

[C]able operators should reasonably be expected to achieve productivity gains in the future analogous to those historically realized by other communications firms. Cable television networks are similar in many ways to telephone networks, and both have benefited from advances in telecommunications technology in the past; both are likely to see benefits in the future, especially as cable and telephone networks converge.¹⁴

The Commission tentatively set a two percent productivity offset for the cable industry. The Commission did offer to give the cable industry "another opportunity" to develop data.¹⁵ The Commission made it clear, however, that "any interested party seeking to justify a different productivity offset will of course be expected

¹² *Id.*

¹³ See, e.g., Declaration of Robert L. Townsend (attached to Joint Comments of Bell Atlantic, The Nynex Telephone Companies, and the Pacific Companies in Response to Notice of Proposed Rulemaking (filed Aug. 25, 1993)); P. Huber, et al., The Geodesic Network II: 1993 Report on Competition in the Telephone Industry (attached to Joint Reply Comments of Bell Atlantic, The Nynex Telephone Companies, and the Pacific Companies in Response to Notice of Proposed Rulemaking (filed Sept. 14, 1993)) ("Report on Competition").

¹⁴ *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation; and Adoption of a Uniform Accounting System for Provision of Regulated Cable Service*, 9 FCC Rcd 4527, 4688 (1994) ("Further Notice").

¹⁵ Further Notice, 9 FCC Rcd at 4688.

to provide reliable, detailed, and credible evidence that some other figure represents the productivity gains, after inflation, that cable systems can reasonably be expected to achieve."¹⁶

In allowing the cable industry one last opportunity to rebut the evidence supporting the proposed offset, the Commission warned that "*cable systems should not expect that their failure to provide any evidence of cable system productivity gains, information they are best able to provide, should justify the conclusion that cable systems cannot reasonably be expected to achieve productivity improvements.*"¹⁷ In spite of this clear warning, the cable industry again failed to submit an industry-wide productivity study. Instead, NCTA submitted a limited study based on only three self-selected companies, which ignored cable's most significant productivity gains.¹⁸ Moreover, as demonstrated in expert testimony submitted in response, when properly evaluated, this study actually shows that productivity growth for cable companies has been as least as high as that of local telephone companies.¹⁹

¹⁶ *Id.*

¹⁷ Further Notice, 9 FCC Rcd at 4688 (emphasis added).

¹⁸ Christensen Associates, Productivity Growth in the Cable Television Industry at 3 (attachment B to Comments of the National Cable Television Assoc. (filed July 1, 1994)).

¹⁹ Declaration of Robert G. Harris in Support of Reply Comments of Bell Atlantic at 3-6 (attached to Reply Comments of Bell Atlantic (filed Aug. 1, 1994)).

Nevertheless, the Commission declined to set a positive productivity offset because the current record "does not provide an adequate factual basis."²⁰

Argument

A. The Record Supports a Productivity Factor Equivalent to One Imposed on the Telephone Industry.

As the Commission recognized, "cable operators should reasonably be expected to achieve productivity gains in the future analogous to those historically realized by other communications firms."²¹ Such a conclusion, which mandates an analogous productivity factor, is well supported in the record.

In fact, the evidence in this proceeding strongly supports the Commission's conclusion that these previously distinct industries are converging.²² The growing reliance on fiber by both the telephone and cable industries is "blurring the lines and

²⁰ Productivity Offset Order at ¶ 7.

²¹ Further Notice, 9 FCC Rcd at 4688.

²² See Further Notice, 9 FCC Rcd at 4688.

increasing competition," between the industries.²³

The cable industry's technological convergence with telephony also coincides with the convergence of services offered. In fact, the record in this proceeding demonstrates that cable companies are already extensively involved in the provision of telephone services.²⁴ This convergence has been recognized by the Commission

²³ **Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992**, MM Docket-215, Joint Comments of Bell Atlantic, NYNEX and the Pacific Companies in Response to Notice of Proposed Rulemaking at 5 (filed August 25, 1993) ("Joint Comments") (quoting Department of Commerce, 1993 U.S. Industrial Outlook). Moreover, this change is coincident with marked improvements in cable's productivity growth. The combination of new infrastructure, economies of scale and compression technology are allowing cable productivity growth to reach new levels. Declaration of Robert L. Townsend, attached to Joint Comments. Greater concentration or clustering of cable systems through purchases or swaps will accelerate that productivity gain. See **Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming**, CS Dkt. No. 94-48, Comments of Bell Atlantic at 3-4 (filed June 29, 1994).

²⁴ "There is growing competition between cable operators and local exchange carriers. Cable operators are major players in the provision of competitive access service to end-users, interexchange carriers and wireless carriers." Declaration of Robert Harris at ¶ 16, attached to **Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992**, MM Docket 93-215, CS Docket 94-28, Comments of Bell Atlantic (filed July 1, 1994) ("Bell Atlantic Comments"). For numerous examples, see *id.* at ¶¶ 16-19; see also Report on Competition at 2.53-2.65.

and the Administration,²⁵ and is only accelerating as cable companies unveil industry-wide plans to buy the telephone technology required for full competition.²⁶

Consistent with this convergence, expert economic testimony submitted in this proceeding demonstrated that the productivity growth rate for the two industries should be equivalent.²⁷ Indeed, to the extent the growth rates diverge in the future, the cable industry's should be higher.²⁸

Other than the failure of the cable industry to provide adequate information, the Commission has only cited one argument for not setting a productivity offset equivalent to that imposed on

²⁵ "[A]s the cable and telephone industries converge, it is important to treat them with as much regulatory parity as possible." *Implementation of Sections of the 1992 Cable Act - Rate Regulation*, 9 FCC Rcd 4119 at ¶ 24 (1994). See also Testimony of Larry Irving, Asst. Commerce Secretary, Before the House Subcommittee on Economic and Commercial Law at 7 (Jan. 26, 1994) ("As Vice President Gore emphasized on January 11, we are moving away from a world where technologically valid regulatory distinctions may be made among local telephone, long distance telephone, cable, and other purveyors of information transmission. . . . Regulatory policies predicated on the old boundaries can harm consumers by impeding competition and discouraging private investment in networks and services.").

²⁶ M. Robichaux, *Cable Operators Plan Big Outlay for Phone Gear*, Wall St. J., Aug. 10, 1994, at B5.

²⁷ Declaration of Robert G. Harris at 9-19 (attached to Comments of Bell Atlantic (filed July 1, 1994)) ("Harris July 1 Decl.").

²⁸ The only productivity study submitted by the cable industry covered only three companies. Nevertheless, when this self-selected sample was measured on a basis comparable to long term productivity studies of the LECs, the results suggest a productivity offset of 3.5% -- higher than current or projected LEC productivity growth. Declaration of Robert G. Harris in Support of Reply Comments of Bell Atlantic at ¶¶ 4-11 (filed Aug. 1, 1994).

telephony. The Commission suggested that in their current networks, "local telephone companies have benefited from advances in computerized local switches, which are not in general use by cable systems."²⁹ While factually true, this observation can only mean that future cable productivity growth *will be at least as high* as productivity growth in the telephone industry. Because the productivity offset is a proxy for *future* productivity *growth*, this difference suggests that as the cable industry changes to the more productive technology already used by telephone companies, cable's relative growth rates will be *higher*.³⁰ The record is clear that the cable industry productivity offset should be *at least as high* as that imposed on the LECs.³¹

B. The Commission Must Evaluate a Cable Productivity Offset Consistently With Its Valuation of An Offset for Other Industries.

In setting price cap policy in other industries, the Commission made a policy determination that it must impose an appropriate productivity offset as part of the price cap formula. As the Commission made clear in its evaluation of AT&T and LEC

²⁹ Further Notice, 9 FCC Rcd at 4688.

³⁰ Harris July 1 Decl. at ¶ 13.

³¹ Even if the failure of the cable companies to heed Commission calls for additional information left an incomplete record, which it did not, the Commission is not free to use this failure as an excuse to ignore the substantial evidence supporting parity in productivity growth. See *Pennsylvania v. Interstate Commerce Commission*, 535 F.2d 91, 96 (D.C. Cir.) ("the best should not be the enemy of the good"), *cert. denied*, 429 U.S. 834 (1976).

price cap regulation, "any form of regulation" like price caps "must take productivity gains into account."³²

Here, there is substantial evidence supporting an offset equivalent to that of the LECs. The cable industry's failure to supply their own corroborating data can not and does not remove the Commission's responsibility to remain consistent with its own precedents and determine the productivity offset based on available evidence. When the Commission felt the record was inadequate to set a LEC productivity measure, the Commission staff created its own study of LEC productivity.³³ Moreover, when multiple measures of LEC industry productivity were deemed inadequate to set an exact offset, the Commission nevertheless relied on its best judgment of a correct productivity offset and, to compensate for its uncertainty, supplemented that offset with temporary safeguards.³⁴

Any uncertainty in the cable productivity offset level is caused by the cable industry's repeated disregard of Commission

³² *Policy and Rules Concerning Rates for Dominant Carriers*, 3 FCC Rcd 3195, 3400 (1988) (emphasis added).

³³ *Policy and Rules Concerning Rates for Dominant Carriers*, 5 FCC Rcd 6786 at ¶ 77 (1990). Unlike the cable industry however, price cap LECs submitted their own comprehensive studies of industry productivity. *Id.*

³⁴ The Commission proposed a rate of return based "backstop" primarily because it found that it lacked "the same degree of corroboration for an average LEC productivity factor" as it had with AT&T." *Policy and Rules Concerning Rates for Dominant Carriers*, 4 FCC Rcd 2873, 2877 (1989). In the current LEC price cap review, the industry has supplied that corroboration in the form of an industry-wide long term total factor productivity study. L.R. Christensen, et al., *Productivity of the Local Telephone Operating Companies* (attachment 6 to *Price Cap Performance Review for Local Exchange Carriers*, CC 94-1, Comments of the United States Telephone Assoc. (filed May 9, 1994)).

warnings about failure to provide productivity data. Rather than place additional safeguards as the Commission did with LECs, the Commission has rewarded the cable industry's intransigence by eliminating the productivity factor altogether.

The Commission has decided that "any industry whose productivity experience differs from [the national norm] will not be accurately represented" in a price cap index without a productivity factor.³⁵ Setting a productivity factor of zero is itself a decision that must be supported by record evidence. Here the record evidence supports a productivity factor equivalent to that applied to local telephone companies.

C. The Commission is Required to Treat the Similarly Situated Cable and Telephone Industries the Same.

Equivalent treatment for the competing and converging telephone and cable industries is not only good policy, it is required by law.

First, from a policy prospective, failure to treat the converging cable and telephone industries on an equivalent basis can only serve to skew investment incentives and distort the competitive marketplace. Ultimately this works to the disadvantage of consumers, who do not receive the same benefits of new services

³⁵ *Policy and Rules Concerning Rates for Dominant Carriers*, 3 FCC Rcd at 3400.

and reduced prices that would flow from full and unfettered competition.³⁶

Second, the D.C. Circuit has continually reminded the Commission of "the importance of treating similarly situated parties alike or providing an adequate justification for disparate treatment."³⁷ The Commission must "do more than enumerate factual differences," it must "explain the relevance of those differences to the purposes of the Federal Communications Act."³⁸ Indeed, the Commission has already been admonished for disparate treatment of cable operators and common carriers. In the context of fines, the D.C. Circuit found that the Commission "cannot determine that common carriers as a class will pay heavier fines" than cable

³⁶ See, e.g., Dr. Harris's discussion of the disastrous results of asymmetrical regulation between the competing railroads and trucking industries. Harris July 1 Decl. at ¶¶ 20-27 "The cautionary lesson of that experience -- and similar experience in financial services and energy regulation -- is that this Commission should adopt policies that promote balanced competition between cable and LECs. Both industries should receive comparable treatment in the implementation of price caps on regulated services." *Id.* at ¶ 27.

³⁷ See, e.g., *McElroy Electronics Corp. v. FCC*, 990 F.2d 1351, 1365 (D.C. Cir. 1993).

³⁸ *Adams Telcom, Inc. v. FCC*, No. 93-1103, slip op. at 9 (D.C. Cir. Oct. 28, 1994) (quoting *Melody Music, Inc. v. FCC*, 345 F.2d 730, 733 (D.C. Cir. 1965)). Regulatory parity is also consistent with the 1992 Cable Act. A principle purpose of that act is to foster meaningful competition so that the marketplace can be relied upon to stimulate video diversity and to discipline cable rates. Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, § 2(b) (1)-(2), 106 Stat. 1460 (1992). Favoring cable over its telephony competitors would undermine that competition.

companies and others and not "explain their reasons for that position or subject that explanation to judicial review."³⁹

Here, there is no justification for ignoring the record and arbitrarily distinguishing between the productivity offset applied to the cable TV and telephone industries.


Conclusion

The Commission's order ignores the record, ignores the Commission's own prior conclusions and ignores the legal mandate that similarly situated entities receive like treatment. The Commission cannot abrogate its responsibilities by setting a productivity offset of zero for cable while retaining a positive offset for local telephone companies. Accordingly, the Commission should reconsider its decision, and mandate an offset for cable that is at least equivalent to the offset it decides upon in the LEC price cap review.

³⁹ *United States Telephone Association v. FCC*, 28 F.3d 1232, 1236 (D.C. Cir. 1994).

Respectfully submitted,

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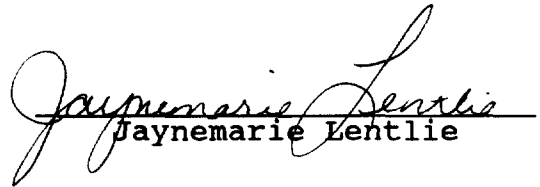

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November 14, 1994

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing "Bell Atlantic Petition for Reconsideration" was served this 14th day of November, 1994, by first class mail, postage prepaid, on the parties on the attached list.


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